NO. 21119

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

SADIE KATZ,

Appellant,

vs.

UNITED STATES OF AMERICA, et al.,

Appellees.

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# BRIEF OF APPELLANT

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APPEAL FROM
THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA

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## JURISDICTION AND FACTUAL BACKGROUND

### STATEMENT OF FACTS BRINGING CASE WITHIN THE JURISDICTION OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF CALIFORNIA AND THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT.

Plaintiff and LEROY J. KATZ were married on or about September 5, 1916, and from that time until the death of LEROY J. KATZ on February 27, 1960, remained husband and wife. That on or about August 24, 1956, a Trust was created wherein LEROY J. KATZ was the Trustor and Title Insurance and Trust Company was the Trustee. Thereafter, on May 5, 1957, and on October 31,

1958, said Trust was amended by Title Insurance and Trust Company and as amended, was in effect when LEROY J. KATZ died.

That subsequent to his death and within the time required by law, a Federal Estate Tax return, Form 706 was prepared and filed with the District Director of Internal Revenue at Los Angeles, California. Following the filing of said return, a Federal Estate Tax examiner determined that a deficiency in said tax existed. The deficiency was paid as assessed, and on June 28, 1963, plaintiff made claim for refund on Internal Revenue Service Form 843, which claim was disallowed. Thereafter, plaintiff filed suit for refund in the District Court of the United States, Southern District of California, Central Division. Cross-motions for Summary Judgment were brought and on February 11, 1966, judgment was entered for the United States of America dismissing plaintiff's complaint with prejudice. Thereafter, and on or about April 5, 1966, plaintiff filed a Notice of Appeal to this Court.

Jurisdiction of the United States District Court for the Southern District of California, Central Division is conferred under Title 28, U.S.C. Section 1346(a)(1). A reference is made to Findings of Fact No. 1 by the District Court.

Jurisdiction to hear this appeal is conferred upon the United States Court of Appeals for the Ninth Circuit by Title 28, U.S.C. Section 1291.

## STATEMENT OF CASE

Plaintiff contends that the additional tax assessed by the defendant, was erroneous in that only one-half of the corpus of the Trust is taxable in the Estate of the decedent, LEROY J. KATZ. The defendant contends that all of the corpus of the Trust is taxable in the Estate of the decedent. The parties agreed, for purposes of the cross-motions for summary judgment, and the trial Court found, that prior to the execution of the Declaration of Trust, the property placed therein was the community property of the decedent and the plaintiff. Reference is made to Finding of Fact No. 10 and Conclusion of Law No. 5. The Trust was established by Title Insurance and Trust Company, by Declaration dated August 29, 1956, which Declaration states that LEROY JOSEPH KATZ, a married man is Trustor. See recitals in Declaration of Trust, I and II, that the Trust was created by the Trustor for the benefit of his wife SADIE KATZ, his children EVELYN JEAN KATZ KLIMAN, and JOSEPH PHILLIP KEITH, the surviving spouses of the Trustor's children, if any, and the surviving issue of his children, as in the Trust more fully provided. SECTION FOUR of the Trust provides,

> "During the lifetime and competency of the Trustor, the Trustee shall have no rights, duties or powers with respect to any property held under this Trust, it being understood that the Trustor retains all such rights and shall collect, receive and disburse without

accounting to the Trustee or any other person, all income of every nature and description from the real and personal property held hereunder."

SECTION THIRTEEN of the Trust provides, "The right if reserved unto the Trustor to revoke, terminate or amend this Trust in whole or in part, at any time or from time to time, by written request therefor, addressed and delivered to the Trustee, provided, however, that no such amendment shall effect the duties, liabilities or compensation of the Trustee, without its written consent."

Under the heading, "Approval of Wife," SADIE KATZ signed the following statement: "I, SADIE KATZ, wife of the Trustor, do hereby fully approve the foregoing Declaration of Trust, No. PP-13003, Dated August 24, 1956. Signed: SADIE KATZ."

Thereafter, on May 5, 1957, and October 31, 1958, the Trust was amended pursuant to Article XIII of the Trust and SADIE KATZ signed each of the amendments under the heading, Consent of Trustor's Wife to Partial Amendment, "I, SADIE KATZ, Trustor's wife, do hereby consent to and fully approve of the foregoing partial amendment to Title Insurance and Trust Company's Declaration of Trust, No. PP-13003, and agree to be bound by the provisions thereof. Dated at Los Angeles, California, April 27, 1957. Signed: SADIE KATZ." and the same statement, dated at Los

Angeles, California on October 27, 1958 and signed by Appellant.

Appellee contends and the Court found, that the legal effect of the approval of SADIE KATZ of the Declaration of Trust, was to part with her interest in the community property transferred to the Trust and to transmute the property of the Trust into the separate property of the Trustor. Reference is made to Finding of Fact No. 10 and No. 11 and Conclusions of Law, No. 3 and No. 5.

Appellant contends that her approval of the trust instrument was not a consent, tacit or express, to a transmutation of her community property to the separate property of her husband. In the alternative, appellant contends that the transfer of the community property of the decedent and appellant did not constitute a transmutation of that property into the separate property of the decedent, because the approval of Appellant of the trust was not a consent to any such transmutation but merely an acknowledgment of her awareness of the terms of the trust instrument and an agreement that as to third persons dealing with the trust she did forego her right to rescind conveyances of real property.

As a further alternative, Appellant contends that the transfer of community property to the trust was avoidable as to her one-half interest therein because made without the advice of independent counsel, and that until cured by her failure to take against the trust after the death of her husband, her share of the property transferred retained its community property character and she remained the owner thereof.

As a further alternative, Appellant contends that the Trust is illusory because the rights retained by the Trustor were so complete that there never was a valid Trust created and that the Trustee received only a bare legal title to the property as the agent of the community.

## SPECIFICATION OF ERRORS

The trial court erred in the following particulars:

1. In finding that there was an intent to transmute the Appellant's community property either tacitly or expressly.

2. In its application and interpretation of prior case law.

3. In finding that appellant's approval was effective upon creation of the trust.

4. In finding that the trust was valid.

## SUMMARY OF ARGUMENT

No intent to transmute Appellant's community property to her husband's separate property can be found tacitly or expressly in the Declaration of Trust.

The issues raised in this case have been previously adjudicated and a proper application of those decisions require a decision for the appellant.

In the alternative, appellant contends that the attempted

creation of the trust was ineffective.

Under either contention, Appellant's property is not subject to taxation in her husband's estate.

## ARGUMENT

The position taken by the Appellee and that adopted by the District Court was that the Appellant assented to a transmutation of community property to her husband's separate property. All parties to this appeal apparently concede that an intent to transmute is necessary.

Just where this intent to transmute is legally disclosed is not clear. Appellant assumes that any such manifestation of intent is predicated upon either (1) Appellant's tacit approval of the benefits she derived from the trust, or (2) her express approval of the terms of the trust instrument.

Appellant will examine each contention.

### I

### CAN APPELLANT'S INTENT TO TRANSMUTE BE FOUND IN HER TACIT APPROVAL OF THE POWERS OF MANAGEMENT CONTAINED IN THE DECLARATION OF TRUST?

It has been the position of Appellant throughout this matter that all of the property of LEROY J. KATZ, decedent and Appellant

was community property. The Court in its Findings of Fact and Conclusions of Law on Defendant's Motion for Summary Judgment (Finding of Fact No. 10, page 3, lines 12 to 15) indicates that the Court assumed that the trust res was community property.

Appellant urges that no tacit assent to a transmutation can be found as a matter of law from her acquiescence to the extensive powers of management reserved in the Trustor (LEROY J. KATZ) during his lifetime. Appellant adopts this argument because of the fact that the powers of management which the Trustor exercised were in fact only reflective of his rights to manage the community property of the community and in fact those same powers were imposed upon him by statute.

To establish this point, Appellant directs attention to Paragraph IV of the Declaration of Trust:

> "During the lifetime and competency of the Trustor, the Trustee shall have no rights, duties or powers with respect to any property held under this trust, it being understood that the Trustor retains all such rights, and shall collect, receive, and disburse, without accounting to the Trustee or any other person, all income of every nature and description from the real and personal property held hereunder."

The pertinent sections of the California Civil Code dealing with those same rights, as they apply to a husband under

community property law are as follows:

"Except as provided in Section 172b, the husband has the management and control of the community personal property with like absolute power of disposition. . . ." (Emphasis added) (Footnote 1 to appendix).

California Civil Code, Section 172.

"Except as provided in Section 172b, the husband has the management and control of the community real property. . . ." (Emphasis added) (Footnote 2 to appendix).

California Civil Code, Section 172a.

"Although under the provisions of Section 161a, Civil Code, the husband and wife have an equal interest in the community property during the continuance of the marriage relation, they do not possess equal powers of management, control of disposition thereof. [Citations]. The husband has the management and control of the community property. . . ."

Sanderson v. Niemann (1941), 17 Cal. 2d 563, 110 P. 2d 1025.

"In accordance with the provisions of Sections 161a, 172 and 172a of the Civil Code, the respective

interests of the husband and wife in community property are existing and equal, subject to the very dominant right of the husband to manage and control such property."

Mosesian v. Parker (1941), 44 Cal. App. 2d 544, 112 P. 2d 705.

By way of comparison, Paragraph IV of the Declaration of Trust establishes an unfettered control of the trust res by the Trustor (LEROY J. KATZ). California Civil Code, Sections 172 and 172a give him (as husband) the exclusive right to manage and control the community property. It is submitted that the rights created by virtue of the Declaration of Trust in the Trustor and those created by statutory authority pursuant to the California Civil Code Sections 172 and 172a are, in fact, the same.

This Court has previously had the opportunity to express the husband's position relative to control of the community property in California.

"It is sufficient to say that the Courts of California have decided that the community property of the husband and wife is subject to community debts and that the management and control thereof is vested in the husband by the law of California as declared by the state legislature and by the Courts. [Citations]."

Hannah v. Swift (1932), 61 F. 2d 307.

Likewise, more recent California cases have maintained the

husband's rights of management and control.

> "The position of the husband, in whom the management and control of the entire community estate is vested by statute, Civil Code Sections 161a, 172, 172a, has been frequently analogized to that of a partner, agent or fiduciary. [Citations]."
>
> Lovetro v. Steers (1965), 234 Cal. App. 2d 461, 44 Cal. Rptr. 604.

In addition to the fact that the husband has control and management of the community, it is interesting to note that a wife's action to set aside conveyances and transfers by a husband during his lifetime are considered to be opposed to the public policy of the State of California.

> "If she could not then have maintained an action against him for the value of her interest in the property which he had given away, it would have been due to the policy of the law to forbid vexatious and unnecessary litigation between spouses, and also upon the ground that during the existence of the marriage the husband has the control and management of the community property of which he cannot be divested except through procedure authorized by statute."
>
> Fields v. Michael (1949), 91 Cal. App. 2d 443, 205 P. 2d 402.

The trial Court has cited three California cases in support of the proposition that Appellant's approval constituted her consent to the transmutation of her community property to her husband's separate property (Conclusion of Law No. 3, page 4, lines 10-18).

It is first to be noted that the "approval" referred to by the trial Court might be either a form of tacit approval found by virtue of the benefits derived by Appellant, or from the written approval signed by Appellant and affixed to the Declaration of Trust.

Assuming that it is the former, Appellant urges that the trial Court erred in its interpretation of the cases relied upon by it to reach its conclusion.

In relying on the case of Kirkwood v. Bank of America (1954), 43 Cal. 2d 333, 339-340, 273 P. 2d 532, the trial Court failed to take into consideration that the taxing statute under construction in that case, Section 13554 of the Revenue and Taxation Code, deals with inter vivos transfers of community property. The section at the time of the Kirkwood case provided as follows:

> "Where community property is transferred within the provisions of Chapter IV of this part, other than by will or the laws of succession from one spouse to the other:
>
> "(a) One half of the property transferred is subject to this part, if the wife is the transferee.
>
> "(b) None of the property transferred is subject to this part if the husband is the transferee."

Thus, the Court in Kirkwood, found that the taxation of community property which had been transferred under a valid inter vivos trust, from the husband to the wife, was to be taxed under the provisions of Section 13554. It did not find that the property was to be taxed as separate property. The difference between the contention of the taxpayer and the Inheritance Tax Appraiser in that case, was as to which method of valuation of the wife's community property interest should be used.

Thus assuming, arguendo, that Appellant made a transfer of her community property interest in approving the trust in this case, the decision in Kirkwood would serve to establish that the interest which she received for that transfer was community property, which under the California Inheritance Tax, a succession tax, was accorded treatment different from transfers upon the death of the husband where the surviving wife elects to take under a Will of her husband in which he disposes of the entire community property (Revenue and Taxation Code, Section 13552) or where the husband disposes of only his one-half of the community property (Revenue and Taxation Code, Section 13551).

In upholding the Inheritance Tax Appraiser's determination, of the tax upon the community property, the Court is saying that the community property interests which the husband and wife received upon the inter vivos transfer to the trust, were to be taxed in accordance with the statutory rules applicable to that type of community property.

Metzger v. Vestall, 2 Cal. 2d 517, 522-523 (1935), 42 P. 2d

67, is the second case cited in favor of the finding that there was a transmutation. This is a case dealing with a wife's express consent to a series of legal instruments all of which had the effect of transferring certain community property interests to the son of the transferors. The Court in the Metzger case found there was consideration for such transfers, but arguendo, and by way of dicta, pointed out that one transferor signed a series of legal instruments illuminating her intent. But, the major distinction is and the Court so found that,

> " . . . the division of the corporate stock at the inception of the corporation was in accordance with an oral agreement or undertaking among the parties that such division should be made in consideration of the spouses transferring to the corporation their community property. . . ." (Emphasis added)

The Findings of Fact and Conclusions of Law signed by the District Court recite in Finding of Fact No. 9, page 3, lines 3 through 9, that there was no underlying oral agreement in the case at bar.

It is therefore to be noted that the Metzger case is not authority for the proposition that the Appellant agreed to transmute.

The third case relied upon the Findings by the District Court was Schindler v. Schindler. The opinion in this case succinctly states:

> "The sole question presented on this appeal is

whether the trial court properly determined that the real property was in fact community property and therefore subject to disposition in the divorce proceedings."

Schindler v. Schindler (1954), 126 Cal. App. 2d 597, 604, 272 P. 2d 566.

The alleged transmutation in this case was that the wife agreed to the transfer of her separate property community property. Manifestly this must be distinguished from a transmutation from community property to separate property because of the fact that the wife in California retains vested rights and interests in the community property.

California Civil Code, Section 161a clearly establishes that Mrs. Schindler had present rights in the community property, and did not divest herself of the opportunity to be awarded a portion of the community property.

"The respective interests of the husband and wife in community property during continuance of the marriage relation are present, existing, and equal interests. . . ."

California Civil Code, Section 161a. (footnote 3 to appendix).

In the case at bar, Appellant would have had no such rights under Civil Code, Section 161a (if there was an effective transmuta-

tion) because there would then be no community property to divide.

It would appear reasonable to assume that the public policy of California is illustratively set forth in the California Civil Code, Section 164 (Footnote 4 to appendix) relating to the presumptions of property being community property and manifests the intent to protect a vested interest of the wife in the community. The Schindler case is not inconsistent with this position since the alleged transmutation was from separate to community property. However, Appellant is being charged with a total divestment of the community property now constituting the trust res. It is submitted that it was error to project a case dealing with the retained interests of a spouse in the community property to a situation where no such rights are found to exist.

## II

## CAN APPELLANT'S TACIT APPROVAL TO TRANSMUTE HER COMMUNITY PROPERTY TO HER HUSBAND'S SEPARATE PROPERTY BE FOUND IN THE FACT THAT SHE MIGHT OBTAIN SOME BENEFIT UNDER THE DECLARATION OF TRUST?

Appellant contends that the applicable sections of the California Civil Code create a responsibility in the husband to support his wife and the benefits derived by Appellant are no greater than her statutory rights. Therefore, it is not consistent to find that she impliedly consented to divesting herself of considerable interests in the community property in an attempt to acquire rights of

support which she was the beneficiary of without recourse to such transmutation.

California law is quite explicit on this point.

"Husband and wife contract towards each other obligations of mutual respect, fidelity and support."

California Civil Code, Section 155.

"If the husband neglects to make adequate provisions for the support of his wife, except in the cases mentioned in the next section, any other person may, in good faith, supply her with articles necessary for her support, and recover the reasonable value thereof from the husband."

California Civil Code, Section 174.

"Every man shall support his wife and his child and his parent when in need. The duty imposed by this section shall be subject to the provisions of Sections 175, 196, and 206 of the Civil Code."

California Civil Code, Section 242.

"The right of a wife to support from her husband arises from the marriage relationship and continues during its existence."

In Re Fawcett's Estate (1965), 232 Cal. App. 2d 770, 43 Cal. Rptr. 160.

III

## IS APPELLANT'S INTENT TO TRANSMUTE EXPRESSLY REFLECTED IN THE DECLARATION OF TRUST?

The Declaration of Trust which is the subject of this litigation indicates on page I that the Trustor is LEROY J. KATZ, a married man. The last page of the Declaration of Trust has the following language:

"APPROVAL OF WIFE

"I, SADIE KATZ, wife of the Trustor, do hereby fully approve the foregoing Declaration of Trust No. PP-13003.

"Dated: Aug. 24, 1956

"s/ Sadie Katz
SADIE KATZ"

Appellant contends that the most reasonable interpretation of the foregoing language is that she approved the Declaration of Trust as to form, and that such language does not reflect Appellant's intention to transmute her share of the community property to her husband's separate property by signing the approval above quoted.

In the Kirkwood case, which the trial Court cites, the Court at page 340, states, " . . . she [the Trustor's wife], with the advice of counsel, signed a formal consent to 'all of the terms and conditions' of the 'Trust Agreement' " (Emphasis added).

Notwithstanding this, the trial Court found that the "necessary legal effect" of the Declaration of Trust was to effect a

transmutation (Conclusion of Law No. 3, page 4, lines 12-14).

Appellant urges that the intent to transmute cannot be found in the benefits derived by her. If, in fact, the trial Court found an express intent to transmute, it could have only been found in connection with the "approval" signed by Appellant. If this is the case, Appellant contends that she should have been represented by independent counsel.

Finding of Fact No. 7, page 2, lines 21 to 24, indicates that Appellant was represented by counsel.

This finding is not supported by the evidence and is not correct. A reading of the Declaration of Trust indicates that the declarant and Trustor was LEROY J. KATZ. The attorney who signed the Declaration of Trust has typed beneath his name these words, "ATTORNEY FOR TRUSTOR". Nothing in the Declaration suggests that Appellant was represented by independent counsel.

By way of illustration of this point, Appellant wishes to develop the analogy of what her rights would have been in attempting to seek a portion of the trust res if a divorce action had been filed by her subsequent to the Declaration of Trust.

If Appellee's position is correct, it would follow that Appellant would be totally foreclosed from obtaining any portion of her share of the former community property.

Most California cases which have dealt with a wife's right to independent counsel have been actions which have been brought by the wife to set aside a property settlement agreement or a default judgment of divorce.

"While it frequently occurs in negotiations between husband and wife for settlement of property matters that one attorney serves both parties, it has been said 'that in fairness to both parties concerned, when negotiations for settlement of property matters between husband and wife are on hand, both parties should at all times be represented by counsel.' [Citations]"

Gregory v. Gregory (1949), 92 Cal. App. 2d 343, 206 P. 2d 1122.

California has apparently even gone beyond the mere necessity of independent counsel. An interesting California case in this area is Vai v. Bank of America National Trust & Savings Assn. (1961), in which it is stated:

"Manifestly, the fiduciary duties and rules governing their performance by a husband should be no fewer or less rigorous than those imposed upon business partners. To hold, as defendant urges, that if a wife employs able counsel upon whom she relies in negotiating a property settlement agreement in conjunction with her action for separate maintenance, that her husband is thereby released from any fiduciary duties in respect to her interest in the community property, would put a wife in a far less protected position than a partner whose partnership is

being dissolved. It would 'permit the authority of the husband in controlling the community property, given him in the interest of greater freedom in its use and for its transfer for the benefit of both himself and his wife, to become a weapon to be used by him to rob her of every vestige of interest in the community property with which the law has expressly invested her. Such a conclusion would violate every sense of justice, and outrage every principle of fair dealing known to the law.' [Citations]"

Vai v. Bank of America National Trust & Savings Assn. (1961), 56 Cal. 2d 329, 364 P. 2d 247, 15 Cal. Rptr. 71, 77.

This Appellant wishes to impress the use by Justice White of the term "able" as it qualifies the word "counsel". Not only is the necessity for independent counsel presumed in the Vai case (which deals with the validity of a property settlement agreement) but the additional qualification of able counsel is present.

## IV

## IF APPELLANT HAS TRANSMUTED HER SHARE OF THE COMMUNITY PROPERTY TO HER HUSBAND'S SEPARATE PROPERTY, WHY WAS SHE ASKED TO APPROVE SUBSEQUENT AMENDMENTS OF THE DECLARATION OF TRUST?

The Declaration of Trust is dated August 29, 1956. On

May 5 of 1957 and October 31, 1958, amendments were drafted and executed by the Trustor, Title Insurance and Trust Company, and Appellant.

The necessary force and effect of the trial Court's position is that on August 29, 1956, the Appellant transmuted all of her interest in the trust res. It would follow then that there would be no need for her to approve of subsequent amendments - the necessary effect of the Declaration of Trust being to negate any rights she had to the trust res and the need to approve any further disposition.

## V

## HAVE THE ISSUES RAISED IN THIS APPEAL BEEN PREVIOUSLY AJUDICATED?

The trial Court's finding (Finding of Fact No. 11, page 3, lines 16-23) is contrary to a prior decision of this Court. In the case of United States v. Stewart, 270 F. 2d 894, 4 A. F. T. R. 2d 2026 (9th Cir. 1959), rehearing denied per curium, 4 A. F. T. R. 2d 6075, this Court considered precisely the same issue as that involved in this case regarding the rights retained by a wife, in insurance policies and annuities purchased with community funds. In the Stewart case, husband and wife were California residents. At the time of the wife's death, there were 26 insurance and annuity policies on the life of the husband, and 7 annuity policies naming the wife as annuitant. The premiums on all of the policies

were paid with community property funds.

The two questions presented to the Court were,

"... (1) whether one-half of the cash value of the 26 policies on the life of the husband was properly includable in the wife's gross estate; and (2) whether all, or one-half, of the proceeds of 5 of the annuity policies in the name of the wife, should be included.

"The question of whether the interest of the wife in her husband's life insurance policies is includable in her estate for tax purposes is determined by the state law of community property [Citations]. Under California law where policies are taken upon the husband's life during coverture, and premiums are paid from community funds, the policies are community property [Citations]."

In its analysis of the insurance policies to determine whether substantial interest therein passed from the wife to the husband, upon the wife's death, the Court found that with respect to 7 of the 26 policies, the husband retained the right to change the beneficiaries, to obtain the cash surrender value and the wife did not consent to the designation of beneficiaries.

With respect to 13 of the policies, the husband retained the right to change beneficiaries and to obtain the cash surrender value, but the wife endorsed the designation of beneficiaries or the mode of settlement.

With respect to two annuity policies, the wife made no endorsement and the husband retained the right to change beneficiaries, but he relinquished the right to obtain cash value. He did, however, retain the right to alter the mode of settlement and to elect to have the policy mature, i.e., to begin to receive monthly installments at an earlier date.

With respect to 4 annuity policies which had matured at the time of the wife's death, pursuant to the settlement agreements, the value of the policies was to be paid in 240 equal monthly installments. The husband was named as first beneficiary, the wife, the second, and others were named as subsequent beneficiaries.

With respect to 3 of these policies, the wife had consented to earlier settlement agreements which were revoked by the husband prior to his execution of the settlement agreement in effect when the wife died. The wife did not sign the settlement agreements which were in effect at her death. With respect to the fourth annuity contract, the husband and wife joined in the settlement agreement.

Referring to the last annuity policy, the Court says:

"In any event, the wife's endorsement did not, in our opinion, constitute a surrender of her interest in the policy. Such a holding would mean that the payments coming to the husband under this contract would be his separate property rather than community property.

"We cannot presume that the wife so intended. . . . It is one thing to hold that a wife's consent to a

beneficiary designation on an insurance policy on the husband's life, means that she gave up her interest in the proceeds of the policy after her husband's death. It is quite another to say that the husband and wife are making a gift of their community interests in the annuity contract when they join in a settlement agreement which has the effect of insuring that the community or the survivor thereof, will receive the annuity payments as long as either is alive."

The holding of the Court in the Stewart case as to each of the types of contract, i.e., insurance or annuity, and whatever the action of the wife in consenting or not consenting, in joining or not joining, and whatever the interests retained by the husband, whether all or partial, that in each case, is one-half of the value of the contract at the wife's death, was includable in her estate. She retained valuable rights in each contract which passed to her husband upon her death.

The Finding of Fact No. 11 and Conclusion of Law No. 5 (reference is made to page 3, lines 16-23 and page 5, lines 22-25, respectively) the last sentence of which Conclusion of Law is as follows:

"The present holding is based on the powers as aforesaid expressly granted to the husband by the Trust instrument and conferred upon him by plaintiff as a result of her consent and approval."

is contrary to the decision of the Fifth Circuit in the case of Commissioner v. The Chase Manhattan Bank, 259 F.2d 231, 2 A.F.T.R. 2d 6363 (5th Cir. 1958). That case involved the collection of gift taxes for gifts alleged to have been made by the wife of her share of community property by her acquiescing in the benefits of three trusts, an insurance trust, a living trust and a testamentary trust, established by her husband. The contentions of the parties as set forth in the opinion of the Court, were as follows:

> "The Commissioner held that on Daniel's death (the husband) the living trust and insurance trust became irrevocable and the testamentary trust came into being. . . .
>
> "(2) As to the living trust, the Commissioner held that it became a completed gift by husband and wife when Daniel died without having exercised his right of revocation. (3) Section 86.2(a) of Treasury Regulations 108, specifically covers insurance payable revocably to a third person and purchased with community funds. The Commissioner held that on the husband's death, there was a gift by the wife of one-half of the amount of the proceeds of the insurance."

Chase Manhattan Bank contended:

> ". . . that Marie (the wife) had made no taxable gifts; but if she had, that the Commissioner's measure of each gift should be reduced by the value of the life

estate she received in her husband's one-half of each trust. . . . (2) As to the living trust and (3) insurance trust, Chase insisted that Marie had no community interest at the time of Daniel's death; her community interest was transferred when the trusts were created in 1928. As in the case of the testamentary trust, Chase claimed that Marie's transfers were 'business transactions . . . for her own benefit.' "

In discussing the life insurance trust, the Court states:

"In a community property state where insurance on the husband's life is purchased with community funds, payable revocably to a third person beneficiary, the husband's right to change the beneficiary and all other control over the property are held as agent of the community. The bundle of rights in the policy are owned by the community. Something happens to this bundle when the insured dies, thereby terminating his control over the property and bringing the community to an end. What happens is, that the community's property interests in the policy-rights are transformed into the beneficiary's rights to the proceeds. It is a shift in control and a shift of beneficial interests. This is the transfer that is taxed.

"Up to the time of his death, Daniel, as managing agent of the community, had the right to change

beneficiaries. When he died without exercising this right, the transfer to the Trustee was a completed gift from the community; one-half therefore should have fallen in the taxable estate of the deceased husband. The other half is a taxable gift from the surviving spouse.

"Under the terms of the Trust Agreement, Marie was the income beneficiary for life. Accordingly, the measure of her gift was half of the amount of the proceeds less a life estate in that half."

In discussing whether the rights received in the inter vivos trust by the husband as sole trustor were separate or community property, the court states:

"It must be borne in mind that Daniel (the husband) did not create the Trust. The community created it. Any rights that were reserved in the settlor were rights held by the community. Newman (referring to Newman vs. Dore, 1937, 275 N. Y. 371, 9 N. E. 2d 966) exercised control over his trust property for himself; Daniel's control (in his case restricted to the right of revocation and modification) could be exercised only as agent for the community." (Emphasis supplied by the Court).

In deciding upon the validity of the living trust, the Court

says:

"We hold that the Moran living trust was not ambulatory; it was a present, valid trust created in 1928. Marie is the income beneficiary under the express terms of that trust and not because she received the income in exchange for relinquishing her half of the community as part of the assumed election to accept the benefits of the trust."

Summarizing its holding, the Court says:

"Our holding does not mean that gift tax consequences attached at the time the trustee took title in 1928. In the transfer of property valid under State law, State law focuses on title. The Federal Gift and Estate tax law focuses on the transfer of the beneficial enjoyment of the property. One who creates a trust during his lifetime, even though he reserves a life estate, parts with legal title to the Trustee and grants to the beneficiaries (including remaindermen) an immediate equitable title. Transfer of the possession and enjoyment of the property may be deferred until some future time. It is this very situation that causes the application of the Gift and Estate Tax laws. Treasury Regulation 108, Section 86.3, provides therefore: 'A gift (for tax purposes) is incomplete in every instance where a donor reserves the power to

revest the beneficial title to the property in himself.'

"The taxable incident is the shifting of the beneficial enjoyment in the trust property, no matter when title is vested.

"Since Daniel retained the power of revocation (for the community), there was no taxable gift until the shift in beneficial enjoyment at his death. [Citations]

"When Daniel died the trust became irrevocable. His community one-half should have been included in his gross estate under Section 811(c) and 811(d) of the 1939 Code, and Marie made a taxable 'gift' of the other half under Treasury Regulations, Section 86.2 and 86.3 less her retained life estate in such half.

"Had Daniel been acting for himself instead of for the community, and had the right of revocation been retained by him individually the taxpayer would have been on stronger ground to urge that, as to Marie, the gift was complete in 1928. But it was as agent for the community, that Daniel held the right of revocation. For tax purposes the gift was incomplete until the right of revocation ceased on Daniel's death."

VI

## IS CASE LAW REGARDING GIFT TAXES APPLICABLE TO ESTATE TAX CASES?

Appellant contends that the Chase Manhattan Bank case, supra, is persuasive authority for the decision of this Court, notwithstanding the characterization of it by the Appellee in the trial Court as inopposite.

Appellant contends that reliance on a case deciding a question of gift tax law is most appropriate for the estate and gift taxes are in pari materia.

> Estate of Sanford v. Commissioner, 308 U.S. 39;
>
> Merrill v. Fahs, 324 U.S. 888.

Beyond that, the Chase Manhattan Bank case of necessity determines the estate tax consequences on the death of the husband as a prerequisite to determining the gift tax consequences to the wife upon his death. As indicated above, "When Daniel (the husband) died, the Trust (the living trust) became irrevocable. His community one-half should have been included in his gross estate under Section 811(c) and 811(d) of the 1939 Code . . .". Moreover, at the inception of the opinion, the Court recognizes that the tax laws of the Federal Government apply to the results obtained under State law, when it says:

> "This case turns on the community property law of Texas. Stated broadly, the question before us is the gift tax effects of trusts and insurance in a

community property state where the wife has a present vested ownership of half of the marital community in her own right."

## VII

## WHEN IS APPELLANT'S APPROVAL OF THE TRUST EFFECTIVE FOR TAX PURPOSES?

The trial Court in Conclusion of Law No. 2 (page 4, lines 7-9) finds the entire trust property taxable in the estate of the decedent LEROY J. KATZ, pursuant to Sections 2036 and 2038 of the Internal Revenue Code. In Conclusion of Law No. 5 (page 4, line 32 to page 5, line 25), the Court distinguishes the case of the United States v. Goodyear, 99 F. 2d 523 (9th Cir. 1938) on the ground that the Goodyear case relies on Section 172 of the California Civil Code, whereas the ruling of the trial court is based " . . . on the powers as aforesaid expressly granted to the husband by the trust instrument and conferred upon him by plaintiff as a result of her consent and approval".

In the Goodyear case, this Court found that a trust agreement was effective to convert California pre-1927 community property into post-1927 community property; and that the powers retained by the husband under the trust were not such as to constitute the creation of a transfer intended to take effect at or after death, such that the entire trust res was includable in his estate.

The Goodyear case stands for the proposition that in

determining the amount of the gross estate of a deceased spouse for purposes of the federal estate tax, state community property law is applicable. The same conclusion is also reached in Lang v. Commissioner, 304 U.S. 264 (1938) and Rickenberg v. Commissioner of Internal Revenue, 177 F.2d 114 (9th Cir. 1949).

Assuming the validity of the trust here in question, appellant contends that the interest in the trust res retained by the trustor and the appellant, even though different from the community property transferred to the trust, was a community property interest and was equal in value to the property transferred. Under the rationale of the Stewart and Chase Manhattan cases, the community interest was held by the trustor and the appellant until the death of the trustor.

> In the words of the Court in the Chase Manhattan case, "It must be borne in mind that Daniel (the husband) did not create the trust. The community created it. Any rights that were reserved in the settlor were rights held by the community . . . . Daniel's control . . . could be exercised only as agent for the community." (Emphasis supplied by the Court).

Appellant contends that if a valid trust was created by the decedent, it was as agent for the community and any revocation thereof would have been for the community. Thus no transfer was made by her until the trust became irrevocable upon the death of her husband.

The trial Court in Finding of Fact No. 12 (page 3, lines 27-29) states,

> "Plaintiff has failed to assert any rights she may have had to withhold her consent or approval or to set aside the trust during decedent's lifetime, or after his death."

If Appellant had the right as she urges she, in fact, did, to set aside the trust during decedent's lifetime or after his death, then a completed transfer was not made by her at the time of the execution of the trust or either of the amendments thereto or at any time during the lifetime of the trustor. Only after the death of her husband, when she failed to exercise her right to set aside the trust as to her community one-half did she make a transfer. The relinquishment of her right to set aside the trust was the act which made the transfer binding as to her and was the taxable event as to her.

Nor does the Kirkwood case require a different result since the Court in that case did not determine, nor was it required to determine, when the consent of the wife to the trust was binding upon her. The statute there in question was a California inheritance tax law applicable upon the death of her husband. Thus, if the husband had revoked the trust, or if the wife had sought to have it set aside during his lifetime or thereafter, the opposite result would have obtained.

Surely if the Appellant had been the first to die, her community interest in the trust res would have been the subject to tax

under Section 2036 of the Internal Revenue Code as a transfer with a retained life estate, and also under Section 2038 as a revocable transfer, in trust, by which the Appellant alone, or in conjunction with her deceased husband, retained the power to alter, amend, revoke, or terminate the trust.

In applying Sections 2036 and 2038 of the Internal Revenue Code to the entire trust corpus, as the trial Court did in its Conclusion of Law No. 2 (page 4, lines 7-9) a further problem is presented since under those sections an incomplete transfer by the decedent is made subject to a state tax. The transfer upon which the Court bases its decision was the creation of the trust, yet the Court held in its Finding of Fact No. 10 (page 3, lines 12-15) that prior to the execution of the trust, the property placed therein was the community property of the husband and wife. Thus, Appellant must have been the transferor of one-half of the trust res, and the decedent could therefore have been the transferor of no more than one-half of the trust res.

In order to maintain a logical consistency, the holding of the Court would seem to require a determination that the transfer to the trust was, in fact, two transfers, first a transfer by the Appellant to her deceased husband by way of gift of her interest in the community property; and then a transfer by the decedent of his half of the community property and the former community property of Appellant to the trust.

It would follow therefrom that Appellant made a taxable gift of her half of the community property to the decedent and is

therefore liable for gift tax on the same property which is subject to estate tax in her husband's estate. Further, as indicated above, upon Appellant's death, the same property will be subject to still another tax under Sections 2036 and 2038 as an incomplete transfer.

Such a grossly burdensome result should not be reached except upon the most compelling reasons. Here the contrary conclusion is the one consistent with the facts and the law, both as previously stated by this Court and the Fifth Circuit Court of Appeals.

## VIII

## WAS THE TRUST VALIDLY CREATED?

The Declaration of Trust approved on August 24, 1956, by LEROY JOSEPH KATZ, provided, inter alia, that the Trust was subject to partial or complete amendment and revocation by the Trustor (KATZ). It further provided that he would have the sole beneficial interest in the Trust during his lifetime. The Trust further provides that:

"SECTION FOUR

"During the lifetime and competency of the Trustor, the Trustee shall have no rights, duties, or powers with respect to any property held under this Trust, it being understood that the Trustor retains all such rights, and shall collect, receive, and disburse, without accounting to the Trustee or any other person,

all income of every nature and description from the real and personal property held hereunder.

"The Trustee shall not exercise any of the powers set forth in SECTIONS ONE, TWO and THREE hereof without first obtaining the written consent of the Trustor, during his lifetime, and after his death, without first obtaining the written consent of all of the adult beneficiaries who are then entitled to receive the income hereunder."

In addition to that, the Trust provides that:

"SECTION FIVE

"Upon the death of the Trustor, the Trustee shall then commence to manage the trust property and shall distribute in monthly installments all net income to SADIE KATZ, the Trustor's wife."

California law clearly recognizes that a Trust will not be found invalid because the Trustor reserves the right to amend or revoke the Trust during his lifetime, and similarly when in addition to that the Trustor also retains a beneficial life interest in the Trust, it will likewise not be found invalid.

Nichols v. Emery, 109 Cal. 323, 41 Pac. 1089 (1895).

The Trust instrument involved in the instant case not only includes the Trustor's reservation of the right to amend or revoke

(SECTION THIRTEEN of the Trust), and the right to retain a beneficial life interest in the Trustor, but also involves a total retention of all of the rights to control the administration of the Trust during the Trustor's lifetime, without any duty to account to the purported Trustee or to any other person, as set forth in SECTION FOUR of the Trust.

California Civil Code, Section 2221 permits the creation of a Trust in real or personal property, by any words or acts of the Trustor indicating with reasonable certainty:

1. An intention on the part of the Trustor to create a Trust; and
2. The subject, purpose and beneficiary of the Trust.

The Declaration of Trust clearly reflects the fact that real or personal property had already been transferred to the named purported Trustee, Title Insurance and Trust Company. However, the mere transfer of property to one designated as Trustee does not create a valid Trust in and of itself, and it is essential that there be a clear manifestation of intent of the Trustor to create a Trust.

California Civil Code, Section 2221;

Gonzalez v. Riis, 171 Cal. App. 2d 473,

340 P. 2d 1015 (1959).

The question herein involved is whether MR. KATZ genuinely intended to divest himself of the ownership of his property and place it in the hands of a Trustee, subject to the terms of the

administration of the Trust. The answer to this basic question can clearly be ascertained from the terms of the Trust instrument. The Trustee's only right, power or duty during the lifetime of the Trustor, was that of a mere custodian of legal title. LEROY KATZ not only retained the right to control the Trust administration but in fact, he retained the right to administer the Trust himself. Therefore, at the time of the purported creation of the Trust, LEROY KATZ was the Trustor, sole beneficiary, and exclusive administrator. The only transfer of interest in the subject property was a mere divestment of the bare legal title.

The foregoing analysis of the terms of this Trust, makes it abundantly clear that MR. KATZ never intended to give up any of the indicia of the ownership of property, save and except for the bare legal title, and even that was at his beck and call any time that he desired to deal with the property, in whole or in part. By virtue of the foregoing terms of the Trust, as set forth in SECTION FOUR and SECTION FIVE, the named Trustee was powerless to restrain or alter any of the conduct in which MR. KATZ may have wished to engage during his lifetime with respect to the property.

A Trust in which the Trustee is a mere depository and has no duties is designated a simple or dry trust (54 Am. Jur. 30, 31, Trusts Section 13 and 48 Cal. Jur. 2d 657, Trusts Section 6). Under such a Trust a beneficiary is entitled to actual possession and enjoinment of the property, and to dispose of it, or to call upon the Trustee to execute such conveyances of the legal estate as he

directs, and the beneficiary has an absolute control over the beneficial interest together with a right to call for the legal title. Ringrose v. Gledall, 17 Cal. App. 664, 121 Pac. 407. It is elementary that the interest of the settlor, the Trustee, and the beneficiary cannot be held by the same individual and result in validly created Trust, as stated in 54 Am. Jur. 47 Trusts Section 35,

> "Where the settlor is the Trustee, the equitable interest must be in another."

Courts will often attempt to resolve ambiguities in the Trust instrument to protect the interests of the beneficiaries not the settlors of Trusts. However, the purported Trust herein involved is a mere sham, because during the lifetime of LEROY KATZ he is the settlor, he is the sole beneficiary and he acts with absolute control and authority in dealing with the property.

Furthermore, the Trust is ambiguous as to the designation of the Trustee. On the one hand the Trust instrument states that Title Insurance and Trust Company has received certain property constituting the Trust res, that as Trustee it has certain powers to manage and control the Trust property (SECTIONS ONE, TWO and THREE of the Trust). On the other hand however, the Trust instrument clearly states that during the lifetime of LEROY KATZ the Trust powers are retained for his exclusive control and that the named Trustee, Title Insurance and Trust Company, shall have no powers, and can perform no acts without his (KATZ'S) written consent. Therefore, nothing more than a simple or dry

trust was created with an attempt to direct the testamentary disposition of the Trust property upon LEROY KATZ'S death.

It is clear that during the lifetime of LEROY KATZ he reserved in totality the right to control the Trust property without accounting to any other person. It is asserted that where the Trustor reserves the right to amend or revoke the Trust and retains a beneficial life interest in it, and also reserves such power to control the Trustee in the administration of the Trust, no effective Trust is created. The purported Trustee is merely the Trustor's agent acting under his direction, and any disposition of the purported Trust property that the Trustor attempts to make at that juncture, is a testamentary disposition. Which, in order to be valid, would require compliance with the Statute of Wills.

The leading case in the United States dealing with the issue of a settlor reserving control over the Trustee in the administration of the Trust is Newman v. Dore, 275 N. Y. 371, 9 N. E. 2d 966. This case involves the rights of a widow in her attack on validity of an attempted transfer by her husband of all his real and personal property. The terms of the Trust involved in that case are stated on page 968 of the opinion.

> " . . . he reserved the enjoyment of the entire income as long as he should live, and a right to revoke the trust at his will, and in general the powers granted to the trustees were in terms made 'subject to the settlor's control during his life', and could be exercised 'in such manner only as the settlor

shall from time to time direct in writing'."

The Court, in its analysis considered the issue of whether or not the transfer was prohibited by the law of the state of New York, and they found it was not. Next, they asked if it was an attempt to evade the law so as to diminish the contingent expectant estate of the wife. The Court concluded that an attempted circumvention of the law would not cause the transfer to be invalid, and that the husband's motive or intent regarding the diminution in the wife's expectancy was an unsatisfactory test of the validity of the transfer of property. The Court adopted a test which asked the question of whether the settlor, divested himself of the ownership of the property, stating at page 969,

> "The test has been formulated in different ways, but in most jurisdictions the test applied is essentially the test of whether the husband has in good faith divested himself of ownership of his property or has made an illusory transfer. The 'good faith' required of the donor or settlor in making a valid disposition of his property during life does not refer to the purpose to affect his wife but to the intent to divest himself of the ownership of the property."

The Trust herein involves not merely the right to control the Trustee and the administration of the Trust, but afortiori it contains a total retention by MR. KATZ of the power to deal with

the Trust property in the same manner that he had dealt with it prior to the transfer and Declaration of the Trust. The only change effectuated by this transaction was a change merely in form and not in substance. The named Trustee did obtain legal title, however that interest in legal title was totally subject to MR. KATZ's wishes because as the Trust instrument indicates in SECTIONS FOUR and FIVE, all of the powers to deal with the Trust property were reserved to MR. KATZ during his lifetime, and none were vested in the named Trustee.

The California courts have not clearly dealt with the question of the validity of a trust where there is a reservation of the power to amend or revoke, a retained beneficial life interest and retained powers to control the Trustee in the administration of the trust. The closest expressions on this issue are found in De Martini v. Allegretti, 146 Cal. 214, 79 Pac. 871 (1905) and Noble v. Learned, 153 Cal. 245, 94 Pac. 1047 (1908). In the De Martini case the decedent deposited certain funds with the third persons directing them to invest the funds in their names. He thereafter wrote them a letter setting forth certain dispositive provisions with respect to the funds to take effect upon his death. The reservation of control involved in this case as disclosed by the evidence included the following:

1. No limit was placed on the amount up to the whole thereof that the settlor could draw;
2. That the third persons were investing and keeping the money in their names for the use and benefit

of the Trustor; and

3. That the Trustor made the written instrument directing the disposition of the funds after his death for the primary reason "to get rid of the necessities of probate proceedings."

The Court held that in view of the circumstances established by the evidence, the transfer to third persons did not create in them any present vested interest or estate in the property, therefore, a valid trust was not created. The Court further found that the direction to dispose of the property upon the settlor's death was invalid because the writing did not comply with the Statute of Wills, therefore, the property remained in the decedent's estate and was subject to the laws of interstate succession.

The Trust instrument involved here is certainly more formal in nature. It sets forth dispositive provisions with substantially greater complexity, and was executed at a time when matters of this type are more complex and sophisticated. The basic elements, however, are here as they were in the De Martini case.

1. There was no limitation on MR. KATZ's power to deal with the Trust property as stated in SECTION FOUR of the Trust, " . . . the Trustor . . . shall collect, receive and disburse without accounting to the Trustee or any other person . . . ."

2. There was a transfer to third persons to hold property for the use and benefit of the Trustor.

However, in MR. KATZ's case, the Trustee did not even have the power to make investments for the benefit of the Trustor; and

3. The Trustor here made a written instrument, instructing the disposition of the funds to named beneficiaries after his death.

Property which fails to be validly transferred by a Trustor in an inter vivos Trust remains in the estate of the transferror. De Martini v. Allegretti, supra. Upon death a valid testamentary disposition must comply with the Statute of Wills, as stated in California Probate Code, Section 50. The Trust instrument does not comply with the Statute, as required, in that it is not subscribed by the testator at the end thereof in the presence of at least two witnesses who must sign as witnesses in the presence of the testator and at his request. The property subject to testamentary disposition would therefore vest in the surviving spouse, pursuant to California Probate Code, Section 201.

> "Upon the death of either husband or wife, one-half of the community property belongs to the surviving spouse; the other half is subject to the testamentary disposition of the decedent, and in the absence thereof goes to the surviving spouse, subject to the provisions of sections 202 and 203 of this code."

It is therefore asserted that in view of the foregoing analysis of the Trust, the Trust was a mere attempt to obtain a testamentary

disposition of the property that did not comply with the Statute of Wills, and one in which the Trustor did not sufficiently divest himself of the ownership and control of the property so as to create a valid inter vivos Trust.

## IX

## IS THE DECISION FOR THE GOVERNMENT REQUIRED TO PREVENT TAX AVOIDANCE?

Appellant wishes to emphasize that this is not a case of tax avoidance. Under the first theory advanced by Appellant, that a valid trust was created which did not result in the transmutation of Appellant's community property, Appellant is liable for a gift tax upon the death of her husband on her community half of the trust res less her retained life estate in that half. She will also be liable for an estate tax upon her half of the trust res transferred subject to her retained life estate; less, of course, a credit for the gift tax paid.

Under Appellant's alternate theory, that the trust is invalid, all of the trust res passes to Appellant and is subject to tax in her estate. Probate Code, Section 201.5 (Footnote No. 5), less, of course, a credit for estate tax previously paid to which Appellant's estate will be entitled.

## CONCLUSION

Appellant contends that the judgment rendered by the District Court dismissing Appellant's complaint should be reversed.

Appellant further contends that Appellant's Motion for Summary Judgment should properly have been granted by the District Court.

The res of the trust has been considered for the purposes of argument to be community property. All parties to this litigation concede that it was necessary for the Appellant to have intended to transmute her interests in the community property to her husband's separate property. In the absence of any such intent, the Appellant's share of the community property could not be includable in her husband's estate.

If there was any intent to transmute, such intent must be found either tacitly or expressly in the approval by Appellant of the Declaration of Trust.

California community property law, Sections 172 and 172a of the Civil Code clearly establish that the husband has the management and control of the community. As a correlative of his rights of management and control, he has the responsibility of supporting his spouse. The necessary effect of the Civil Code sections is such that Appellant had no right to superimpose her management and control of the community funds. Since these rights were statutory, Appellant urges that her conclusion be sustained that Appellant's alleged intent to transmute is not found in her

acquiescence to those rights established for her benefit under applicable California law.

The trust instrument is clear in that there is no express intent manifesting a clear indication that Appellant was willing to, or did, transmute her share of the community to her husband's separate property. The approval which Appellant signed can reasonably be interpreted as an approval only as to the form of the Declaration of Trust. Even assuming that it was an approval as to substance, such approval would be consistent with the previously discussed duties that she has to respond to the management of her husband. But what is of even greater significance in this case is the fact that Appellant is alleged to have converted her share of the community property to her husband's separate property without the benefit of independent counsel.

The settled California case law is consistent with the position of Appellant and inconsistent with the decision of the trial Court on this point.

The issues in this case have been previously adjudicated by this Circuit Court of Appeals in the case of United States v. Stewart and United States v. Goodyear and in the Court of Appeals for the Fifth Circuit in the case of Commissioner v. Chase Manhattan Bank.

Stated succintly, those cases establish that the interests of a wife in a community property state must be determined under local law; the tax law is applied to the results as determined under local law.

acquiescence to those rights established for her benefit under applicable California law.

The trust instrument is clear in that there is no express intent manifesting a clear indication that Appellant was willing to, or did, transmute her share of the community to her husband's separate property. The approval which Appellant signed can reasonably be interpreted as an approval only as to the form of the Declaration of Trust. Even assuming that it was an approval as to substance, such approval would be consistent with the previously discussed duties that she has to respond to the management of her husband. But what is of even greater significance in this case is the fact that Appellant is alleged to have converted her share of the community property to her husband's separate property without the benefit of independent counsel.

The settled California case law is consistent with the position of Appellant and inconsistent with the decision of the trial Court on this point.

The issues in this case have been previously adjudicated by this Circuit Court of Appeals in the case of United States v. Stewart and United States v. Goodyear and in the Court of Appeals for the Fifth Circuit in the case of Commissioner v. Chase Manhattan Bank.

Stated succintly, those cases establish that the interests of a wife in a community property state must be determined under local law; the tax law is applied to the results as determined under local law.

The Stewart and Chase Manhattan Bank cases establish that the wife retains substantial interests in community property transferred either into insurance or annuity contracts, or into an inter vivos trust; and that those rights persist until the death of the husband or the wife, transmutes them. Thus, it is the death of the first spouse which is the taxable event.

Assuming, arguendo, the validity of the trust established, it follows that Appellant's rights to the community property remained unchanged until the death of her husband so that only one-half of the trust res is properly includable in the taxable estate of her husband; the other one-half of the trust res being taxable to Appellant under the gift tax law to the extent by which that one-half exceeds her retained life estate therein.

It is settled law that the gift and estate taxes are in pari materia; and that the application of decisions in gift tax cases is appropriate in this appeal.

It is contended that the attempted transfer of the community property to Title Insurance and Trust Company did not form the basis for the creation of a valid trust by LEROY J. KATZ. The fatal defect arose out of the reservation by MR. KATZ of the total right to deal with the property to the exclusion of the vesting of any of the rights of control in the designated trustee during MR. KATZ's lifetime. The establishment of a trustee with bare legal title and without any right or power with respect to the property created a dry trust which vested no interest in the trustee as set forth in the California case of Ringrose v. Gledall, supra.

In addition, the attempted transfer with the reservation of the aforesaid control over the subject property was illusory. When an owner of property transfers legal title to a purported trustee with a complete reservation of control over the administration of the trust, there is no real intent to divest one's self of the ownership. This principle is supported by the decisions of Newman v. Dore, supra and De Martini v. Allegretti, supra.

In the instant case, MR. KATZ retained every indicia of ownership except for the mere divestment of the bare legal title to the property and in substance during his lifetime he was the settlor, the trustee and the sole beneficiary.

The trust instrument not only failed to establish a valid trust but was also invalid as a testamentary disposition of the property.

The Statute of Wills is embodied in California Probate Code, Section 50. It is demonstrated on the face of the instrument that there is clearly a lack of compliance with this code section resulting in an invalid attempt to make a testamentary disposition.

The tax result under this theory is that one-half of the trust res only, is taxable in the estate of MR. KATZ and that upon the death of Appellant the entire trust res will be taxable in her estate less, of course, a credit for estate taxes paid in MR. KATZ's estate upon his one-half of the trust res.

Respectfully submitted,
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LEVINSON, MARCUS & BRATTER
By: BURTON S. LEVINSON
Attorneys for Appellant.

## CERTIFICATE

I certify that in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

/s/ Burton S. Levinson

BURTON S. LEVINSON

# APPENDIX "A"

## Footnote No. 1

## Civil Code, Section 172

Except as provided in Section 172b, the husband has the management and control of the community personal property, with like absolute power of disposition, other than testamentary, as he has of his separate estate; provided, however, that he cannot make a gift of such community personal property, or dispose of the same without a valuable consideration, or sell, convey, or encumber the furniture, furnishings, or fittings of the home, or the clothing or wearing apparel of the wife or minor children that is community, without the written consent of the wife.

## Footnote No. 2

## Civil Code, Section 172a

Except as provided in Section 172b, the husband has the management and control of the community real property, but the wife, either personally or by duly authorized agent, must join with him in executing any instrument by which such community real property or any interest therein is leased for a longer period than one year, or is sold, conveyed, or encumbered; provided, however, that nothing herein contained shall be construed to apply to a lease, mortgage, conveyance, or transfer of real property or of any interest in real property between husband and wife; provided,

also, however, that the sole lease, contract, mortgage or deed of the husband, holding the record title to community real property, to a lessee, purchaser or encumbrancer, in good faith without knowledge of the marriage relation shall be presumed to be valid. No action to avoid any instrument mentioned in this section, affecting any property standing of record in the name of the husband alone, executed by the husband alone, shall be commenced after the expiration of one year from the filing for record of such instrument in the recorder's office in the county in which the land is situate, and no action to avoid any instrument mentioned in this section, affecting any property standing of record in the name of the husband alone, which was executed by the husband alone and filed for record prior to the time this act takes effect, in the recorder's office in the county in which the land is situate, shall be commenced after the expiration of one year from the date on which this act takes effect.

Footnote No. 3

Civil Code, Section 161a

The respective interests of the husband and wife in community property during continuance of the marriage relation are present, existing and equal interests under the management and control of the husband as is provided in sections 172 and 172a of the Civil Code. This section shall be construed as defining the respective interests and rights of husband and wife in community property.

Footnote No. 4

Civil Code, Section 164

All other real property situated in this state and all other personal property whatever situated acquired during the marriage by a married person while domiciled in this state is community property; but whenever any real or personal property, or any interest therein or encumbrance thereon, is acquired by a married woman by an instrument in writing, the presumption is that the same is her separate property, and if acquired by such married woman and any other person the presumption is that she takes the part acquired by her, as tenant in common, unless a different intention is expressed in the instrument; except, that when any of such property is acquired by husband and wife by an instrument in which they are described as husband and wife, unless a different intention is expressed in the instrument, the presumption is that such property is the community property of said husband and wife and that when a single family residence of a husband and wife is acquired by them during marriage as joint tenants, for the purpose of the division of such property upon divorce or separate maintenance only, the presumption is that such single family residence is the community property of said husband and wife. The presumptions in this section mentioned are conclusive in favor of any person dealing in good faith and for a valuable consideration with such married woman or her legal representatives or successors in interest, and regardless of any change in her marital status

after acquisition of said property.

In cases where a married woman has conveyed, or shall hereafter convey, real property which she acquired prior to May 19, 1889, the husband, or his heirs or assigns, of such married woman, shall be barred from commencing or maintaining any action to show that said real property was community property, or to recover said real property from and after one year from the filing for record in the recorder's office of such conveyances, respectively.

As used in this section, personal property does not include and real property does include leasehold interests in real property.

Footnote No. 5

Probate Code, Section 201.5

Upon the death of any married person domiciled in this State one-half of the following property in his estate shall belong to the surviving spouse and the other one-half of such property is subject to the testamentary disposition of the decedent, and in the absence thereof goes to the surviving spouse: all personal property wherever situated and all real property situated in this State heretofore or hereafter acquired:

(a) By the decedent while domiciled elsewhere which would have been the community property of the decedent and the surviving spouse had the decedent been domiciled in this State at the time of its acquisition; or

(b) In exchange for real or personal property, wherever situated, acquired other than by gift, devise, bequest or descent by the decedent during the marriage while domiciled elsewhere.

All such property is subject to the debts of the decedent and to administration and disposal under the provisions of Division 3 of this code.

As used in this section personal property does not include and real property does include leasehold interests in real property.